Ontario

FUTURE SCENARIOS FOR ONTARIO

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Multinational Corporations

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Abstract:

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This report considers the conditions that encourage the relative growth or stagnation of such enterprises and postulates certain situations and trends that could prevail over the next couple of decades. The likelihood of occurrence of these trends and some advantages and disadvantages of this are dealt with.

Future prospects for multinationals are considered under low- and high-growth scenarios. Policy implications and recommendations for Ontario are discussed.

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-- Multinational Corporations --

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FOREWORD

As part of the Transportation Outlooks project, seven papers were commissioned, dealing with well-defined themes of major significance to the future development of Ontario. Under the main heading Future Scenarios for Ontario, the titles of the papers are as follows:

1/ The Environment
2/ Resources Sector
3/ Production
4/ Multinational Corporations
5/ Social Values and Behaviour
6/ Political Change
7/ Preliminary Assessment of New Technologies

The papers were commissioned from experts, several of them of national or international renown, in various fields. It is expected that their work, and additional material related to it, will be used in the development of a number of alternative scenarios of Ontario's prospects. The main objectives are to stimulate thinking about the future and to elicit feedback from MTC planners and other users of such information in order to guide further studies of the future, that are both relevant and timely.

It should be noted that these papers, which were completed in June 1982, are primarily the speculations or opinions of experts, not statements of fact. It should also be clear that a different choice of experts would have produced another set of opinions. Part of the process of anticipating future change is the painstaking analysis of detail, including quantitative information, and the expert assessment of emerging and disappearing trends and other qualitative information. Another part is the careful integration and synthesis of all these different types of information. Futures research requires the involvement and participation of all users to improve on the application of futures information to current decision-making.

Most of the reports delineate events as they would develop if Ontario, Canada, and the world were to follow two broadly different futures: low growth and high growth, as described in the following.

Low Growth

This future assumes an economic environment characterized by continued slow economic growth and attempts to reinforce the existing industrial structures globally and locally. The gap between North and South continues to widen and there is little change in conditions in the Third World. Also, relations between East and West continue to be strained. At the same time, attempts to liberalize trade and capital movements as well as reform the international monetary system will be piecemeal and sporadic.

High Growth

The main features of this environment are more rapid economic growth and attempts to harness the new technologies (e.g., micro-electronics, biotechnology, oceanography, etc.) in building a new industrial structure globally and locally. The assumptions include greater co-operation between East and West, and North and South, with rapid improvements in the conditions of the Third World. At the same time, there will be strong and relatively successful attempts to liberalize trade and capital movements as well as reform the international monetary system.

Two of the reports are based on different pre-conditions. In the case of Preliminary Assessment of New Technologies, the two scenarios were simply omitted, and an assessment was done of the potential of developing a high-technology future for Ontario. The paper Political Change deals with two main scenarios and a third scenario which considers an overlay on each of the preceding two. One pre-condition -- in effect, an amalgamation of two alternatives -- was given for this paper and is as follows.

Assume a competitive world environment (politically and economically) with slow rates of economic growth for most nations, a high priority for more economically successful countries to re-industrialize using high technology, and serious international competition for resources and markets. There will be winners and losers nationally, as well as by and within industrial sectors.

ABSTRACT

The purpose of this paper is to consider the future of multinational corporations in Canada, with a specific appraisal of their future in Ontario over the long term, that is, towards the end of the century.

This report considers the conditions that encourage the relative growth or stagnation of such enterprises and postulates certain situations and trends that could prevail over the next couple of decades. The likelihood of occurrence of these trends and some advantages and disadvantages of this are dealt with.

Future prospects for multinationals are considered under low- and high-growth scenarios. Policy implications and recommendations for Ontario are discussed.

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1/ INTRODUCTION

A multinational corporation is broadly defined here as an entity that establishes and maintains activities that contribute to the production of goods and services in more than one national jurisdiction.

The purpose of this paper is to consider the future of multinational corporations in Canada generally, but with some specific appraisal of their future in Ontario over the long term, that is, towards the turn of this century.

For this to be a relevant and useful speculation, it is first necessary to consider the conditions that encourage the relative growth or stagnation of such enterprises, and then, to postulate certain assumptions about the relevant conditions that could prevail over the next couple of decades.

On the basis of these considerations, two alternative scenarios of world development are outlined, and some conclusions are suggested about the implications of the future course of evolution of multinationals under each scenario for Canada and Ontario. The two scenarios are:

1/ a low-growth, traditional pattern of re-industrialization and structural economic change; and

2/ a more dynamic, technologically-oriented, investment-intensive and skill-intensive pattern of future growth and change.

2/ CURRENT SITUATION

2.1/ Factors Influencing the Growth or Stagnation of Multinationals

The essential keys to understanding the possibilities for growth of multinationals relate, in a somewhat over-simplified way, to three basic circumstances.

1/ The first and, perhaps, most basic set of factors concerns disparities in the availability of productive factors between national economies, and the possibilities for transfer of these factors from "more-enriched" to "less-enriched" environments. An appropriate analogy is, perhaps, the flow of air from "high-pressure areas" to "low-pressure areas." From its earliest days, Canada has experienced such transfers of productive resources, starting with the Hudson's Bay and the North-West Companies and, subsequently, stretching through many parts of the early stages of Canadian economic development. An especially heavy emphasis was placed on resource development and related commercial, transportation, financial and other associated activities. Canada, in fact, is a classic case of a "large and largely-empty land" in which economic development and progress depended vitally on a "vacuum-type sucking in" of foreign capital, manpower, skills, experience, risk-taking capacities, access to external markets, imports of needed goods and services and inflows of managerial, technological and other know-how. At about the same time (from the mid 19th century through at least the early part of the 20th century) that Canada began to experience these large net inflows of the essential ingredients for economic progress -- sometimes briefly encapsulated in the term, "men, materials and money" -- other nations, such as Argentina, India and Australia, also had similar opportunities. But for a variety of reasons, Canada managed to benefit most from the "total package" of productive input transfers, perhaps because it had, in the conditions of those times, a clearer advantage in being able to export goods and services to pay, internationally, for these transfers. (In this context, incidentally, it should not be forgotten that the United States, in the 19th century, was also a major importer of foreign productive resources and had accompanying access to export markets, especially from the United Kingdom, at least over the middle to latter part of the last century.)

2/ A second set of factors concerns the terms and conditions under which such resource transfers can be made. Obviously, high costs and/or constraints on such transfers will limit them. More open conditions will foster a larger scale of multinational activities and structures. Thus, the deliberate efforts to "open up" the world system for trade and capital, and technological and other productive factor flows in the quarter century after World War II provided a highly favourable climate for the rapid growth and development of multinational organizations and activities. Moreover, the Marshall Plan and other U.S. efforts to foster post-war, economic reconstruction in Europe (and, to a lesser extent, Japan), together with such subsequent developments as the formation of the European Economic Community, greatly encouraged the growth of multinational corporations.

3/ At the other end of the spectrum, there are highly "closed conditions" that may foster the spread of multinational activities. Again, Canada provides a highly illustrative example: under the constricted set of international economic conditions of the 1930s, with high barriers to imports of goods, there was a clear invitation to foreign multinationals to "take up residence" in Canada. (This was welcomed by Canada, which was suffering at the time from high unemployment, stagnating growth of productivity and real incomes, and severe balance-of-payments and exchange-rate strains.) Moreover, in the 1930s, this influx of foreign multinationals was further promoted by Canada's initiative in 1932 to establish a British Commonwealth preferential tariff system which not only gave Canadian subsidiaries of U.S. and other firms access to the protected, if small, Canadian market, but also the wider markets of the Commonwealth.

Two other basic considerations about multinationals (at least, about large multinationals) are important to keep in perspective.

1/ Because of their size and the diversity of their operations, they have much larger capacities to take risks. The economic risks of <u>major new</u> mining, manufacturing and other ventures are quite high. A very large multinational firm is typically in a better position to assume such risks than a small national enterprise, even if the latter's risk is shared partly (or even wholly) by national governmental involvement.

2/ At least in the post-war period, the typical pattern of multinational growth has not been in the form of moving from "more-developed" to "less-developed" economies (in spite of widespread perceptions that this has been so). The great bulk of multinational enterprise development has been among the industrially-advanced countries. Aside from the "resistance" of less-developed countries to multinational involvement ("intrusions" and "exploitations") in their development, greater economic advantages exist for rising multinational operations among more-developed countries. It has been among these countries that the greatest opportunities have emerged for increasingly-sophisticated and effective initiatives in the development of transnational activities, in the context of strong market growth and substantial structural economic change.

This second consideration, incidentally, has a very important corollary: in today's world, there are very few of the large multinational companies that could not afford to absorb the loss (although, perhaps, not without some degree of "pain") of their subsidiary operations in any developing country. Even in the case of Canada, many of the very large multinationals appear to have only about 5% to 10% of their activities here. A loss of those activities (in part, or even entirely, for whatever reason) would not typically be crippling.

A further corollary is that if Canadianization policies and actions were to move towards some degree of expropriation of multinational activities in Canada, the ultimate result would probably be not so much to injure the major multinationals, as to injure Canadians, in at least three major ways.

1/ It would deprive Canada of some inflows of "packages of benefits" that tend to flow from multinational involvement in economic development processes. (Canada is still developing. Indeed, any concept of economic development requires that a country should always be in a "developing situation.")

2/ It would "cost" Canadians a much higher price, than would otherwise have been the case, for goods, services, capital, technology, etc., that are needed for economic progress. (Among the most obvious ways in which such costs would be imposed is through higher capital costs and a lower exchange rate.)

3/ It would "cost" Canadians, on the opposite side, through increased tendencies for Canadian resources (capital, manpower, skills, technology, etc.) to leave this country for what would be perceived to be "more favourable conditions" in other jurisdictions (possibly even to the point of having some Canadian-owned and -controlled corporations move out of Canada to become multinationals in a foreign jurisdiction).

In the main, during the post-war period, Canada has maintained an environment favourable to the development of foreign multinationals. It has also maintained conditions favourable to the "patriation" of ownership and control of what once were "foreign multinationals" to "Canadian multinationals," e.g., Alcan, International Nickel Company (INCO), Canadian Pacific Railways, and the Hudson's Bay Company. But in the changed climate and circumstances of the 1970s, there has been a clear shift, for the first time in recorded Canadian history, to substantial net outflows of direct investment (i.e., "ownership and control" capital) from Canada. Moreover, there are emerging signs that foreign multinationals operating in Canada, as well as Canadian multinationals operating outside of Canada (even wholly domestically-owned and -controlled Canadian enterprises) are considering, with a growing degree of relative favour, centering their main future development in other jurisdictions.

Does this signify the beginnings of new trends that are emerging as the "lagged end-result" of the Foreign Investment Review Agency (FIRA), the National Energy Policy and the relative deterioration in the environment for multinational growth in Canada? It is too early to assess this basic question adequately. However, it is possible to say is that foreign investment in Canada is now "costing" Canadians, in economic terms (partly in higher total payments on interest and dividends), more than it would have in the absence of Canadianization policies, and that net foreign direct capital outflows are now significant and rising (even apart from the special situations of the major "acquisition" and "merger" decisions of 1981, which partly reflected increased merger activity within both countries, that obviously "spilled across the border").

In 1981, net direct capital outflows were over $10 billion, approximately half of which represented withdrawals of equity capital by non-residents, and the other half of which represented Canadian equity investment in foreign companies. Transactions by multinational companies were a dominating feature of these outflows. Because Canada was running a current account deficit, all of this net direct capital outflow, plus an additional substantial amount, had to be funded by capital inflows in the form of fixed-interest obligations (bonds, loans, etc.) in order to retain approximate "balance" in the overall international payment accounts. In brief, this implies that equity (or risk-taking) capital is being replaced by passive, high-interest-cost capital in the structure of Canada's international indebtedness. If this were to continue on a substantial scale into the future, against a background of continuing chronic deficits in Canada's current account balance of payments, the result would be that Canada's structure of international indebtedness would gradually become more like that of large developing countries in today's world, that is, with an overwhelming preponderance of fixed-income indebtedness. An important consequence would be a diminished capacity to operate independent domestic policies.

Finally, with respect to conditions that influence the growth or stagnation of multinational enterprises, it is important to focus again on the central issue of "risk-taking." Multinationals, by nature and experience, are organizations that are constructed, even more than national enterprises, to "deal with uncertainty and reckon with risk." But if changes in their business environment, either in their domestic or international locations, raise economic, political or other risks, their response is likely to be cautious. While risk-taking capacities of many multinationals may be high, "risk aversion" is also a central factor in their decisions and operations. Thus, national actions that are perceived to increase risks are inimical to their progress and development.

2.2/ Host Country Concerns About Multinational Operations

Over the past couple of decades, there has been rising concern that the operations of multinationals may not be fully in accord with national objectives and aspirations in host countries, or, more pointedly, that such operations may adversely affect the capacity of host countries to control and influence the development of their domestic economic, social, cultural and political environments. Such concerns cover a wide field of policies and actions that may be determined in foreign "decision centres." Some of these are business decisions and actions affecting, for example, purchasing policies, technological change and the management of public affairs. Others are foreign government policies affecting parent company operations -- given various corporate linkages with subsidiaries, these can serve as conduits for bringing the influence of such policies to bear on activities in other countries.

In these circumstances, many countries have taken steps to encourage a maximum alignment of subsidiary operations to serve their national interests and needs, for example, through:

- the adoption of "guidelines for good corporate citizenship";

- limitations on the degree of foreign ownership or control of certain key sectors or industries;

- screening processes of various types to achieve maximum national benefits (in relation to costs) from new or existing foreign direct investment; and

- intricate contractual relationships between host governments and multinational corporations, setting forth precise terms and conditions affecting both their structure and conduct.

In the wider international arena, other initiatives have also emerged (through the Organization for Economic Co-operation and Development (OECD), the United Nations, and other international bodies) to seek broad international agreement about appropriate guidelines and regimes for the operations of multinationals.

The consequences of these efforts to influence the operations of multinationals are becoming increasingly entangled with trade policy issues and international trade commitments. They are also, undoubtedly, having effects on the international monetary system, international financial markets and exchange rate relationships, although these have been less clearly identified and analysed.

Under virtually any future scenario, it is highly probable that there will be further national and international initiatives to influence the operations of multinationals in host countries. In parallel, there is likely to be a further escalation in the entanglements noted above.

2.3/ Some Basic Trends

There are three basic trends in multinational activity that are likely to continue to increase in prominence over the next two decades.

1/ If market values of equity continue to remain low in relation to book values, increased merger activity and increased equity positions in companies already partly owned by others will undoubtedly continue, especially in the case of companies in which cash flows are relatively large. In a depressed economic environment, great business power accrues to corporations that have significant cash flows, even if they also have relatively low earnings ratios.

2/ More vertical integration, backward to the sources of materials and components (perhaps, especially by Japanese, South Korean, European and other manufacturers) and forward to capture customers, is likely.

3/ Global product development and marketing could well become increasingly widespread, especially in conditions of increasing robotization and lengths of production runs, in efforts to keep down unit costs, increase productivity and achieve highly-competitive performance.

While this may mean increasing centralization of many key aspects of corporate planning and decision-making, it could also go hand in hand with increasing "transnational" activities and structures, with, for example, more interfacing between boards of directors of companies with many international units, and widening mixtures of managerial, functional and professional personnel from various countries in different locations. Rapid advances in telecommunication and computer technology are also likely, on balance, to exert centralizing tendencies.

2.4/ Some New and Prospective Issues

A number of more speculative questions are emerging about multinationals. Among these, three are singled out here for special attention:

1/ whether "co-operative models" of multinationals may grow significantly?

2/ whether new dynamism may emerge from the establishment and growth of multinationals based in newly-industrializing countries, especially among Pacific Basin nations?

3/ whether multinationals could become an increasingly useful vehicle for encouraging new venture capital financing and the more rapid development of new and smaller enterprises in the countries in which they operate?

1/ First, in recent years, there have been various instances of "co-operative linkages" between national and multinational firms and among multinational firms, for example, between European and Japanese companies in the automobile and electronics industries. It is interesting to speculate whether this may signal the beginning development of "co-operative models" of multinationals, involving diffused ownership, but closely co-ordinated managerial control.

Conceived benefits from such merged structures could be:

- greater opportunities for rationalization, specialization and production operational efficiencies;

- increased capacities for effective market penetration, increased market shares and improved competitiveness;

- more effective development, adaptation and deployment of new product and process technology; and

- the creation of stronger and better-balanced managerial capabilities.

Of course, there is nothing particularly new in the concept of international joint venturing, but substantially increased "joint multinational corporate venturing" could add major new dimensions to such activities.

Such multinational interlinkages could be spurred in a low-growth, reindustrialization scenario, as well as in a rapidly- and technologically-changing, high-growth scenario. But such organizational structures would undoubtedly experience the typical tensions and strains that have been widely experienced by shared-control, joint-venture operations, and it would appear unlikely that any substantial wave of multinational development along these lines will take place in Canada or Ontario over the next couple of decades.

2/ Second, by the year 2000 it is possible that a new wave of multinational development could emerge from relatively fast-growing and maturing industrial nations, especially in the Pacific Basin, and, perhaps, from oil-rich countries having substantial balance-of-payments surpluses. Already noted has been the probability, especially under world, high-growth conditions, of increased vertical integration backward to Canadian resources from such resource-poor countries as Japan, South Korea and Taiwan which may be anxious to establish assured bases of supplies of natural or semi-processed industrial materials, as well as of energy. But there is also the intriguing question as to whether there could emerge a significant wave of investment from these and other countries into multinational manufacturing activities in Canada.

In the next decade or two, it seems highly unlikely that any of today's developing countries will develop significant multinational operations

in Canada. If such development occurs, it is more likely to be among themselves or directed towards lower-cost, still less-developed countries. Also, direct capital investment in Canada, utilizing surplus foreign earnings by oil-rich countries (to the extent that it occurs), is likely to take a rather passive form akin to "portfolio investment."

But Japan may be a different situation. In the 1970s, the main external development of Japanese manufacturing industries has been directed, and even then, on only a relatively limited scale, to other nations in the Pacific Basin; there has been little interest in extending multinational structures into Canadian manufacturing. However, the following possibilities could begin to alter this.

- Under both low- and high-growth scenarios, Canada is likely to become a relatively low-labour-cost country vis-a-vis Japan.

- Under low-growth conditions accompanied by increased trade protection, the attractiveness of establishing or acquiring Canadian manufacturing facilities to develop or maintain a Canadian market position may rise for various Japanese industries.

- Under a low-growth scenario, there may not only be opportunities to acquire Canadian operations on what seems to be a "bargain basis," but there could also be encouragement from governments (and other sources) to "invite Japanese participation" in Canadian industry, especially as a means of supporting employment and, potentially, promoting Japanese contributions to improved industrial productivity performance.

Thus, an increased and more-diversified, Japanese, multinational presence in Canada over the next two decades is highly probable, although its extent and pattern will be influenced by many complex issues regarding various multinational opportunities available to Japanese industry on a global scale.

3/ **Third**, many large multinationals over the past couple of decades have developed initiatives, in varying ways, to use their resources to promote and develop new and small business, especially "venture capital business," in various jurisdictions in which they operate. The results

have not always been successful. (It is interesting to note that when cashflow pressures and cost-containment programmes have been implemented by multinationals, relatively heavy restraints have frequently been placed on their venture capital activities; in some instances, even divestiture of these activities has occurred.) However, important potentials for the utilization of multinational capabilities, such as the mobilization of resources, the application of managerial know-how, and the absorption of risk, will exist, and may increase substantially. This will extend the horizons of new economic development by encouraging new and promising smaller business operations.

Unfortunately, in Canada, FIRA appears to have been a deterrent to such activities. But in a more open environment, and particularly in a high-growth, more technologically oriented scenario, substantial potentials could readily exist for multinationals to play a more dynamic role in new business venturing.

3/ LOW-GROWTH SCENARIO

3.1/ Key Features

The following key features would likely be reflected in the low-growth scenario, to the year 2000:

- low growth for Canada as a whole in an international environment of slow economic growth;
- unstable economic and financial conditions, including more frequent and pronounced business cycles, and fluctuations in interest rates and capital costs;
- relatively high and persistent unemployment (especially of younger and less-experienced people) and periodic substantial under-utilization of production facilities;
- intensified international trade competition, slowly-growing real world trade, instabilities in international capital markets and capital flows, and a widening use of non-tariff trade barriers;
- relatively low growth in real personal income per capita, real consumer spending and real personal saving (no consumer booms);
- persistent strains on governments, where real revenues will be growing fairly slowly, real expenditures will be pressing against fiscal limits, and capacities to establish significant new programmes will be strictly limited (unless some existing programmes are curtailed or eliminated);
- relatively small business profit margins, both in terms of returns on assets and returns on sales, and business savings (retained earnings and depreciation) generally not favourable for modernization and expansion of production facilities;
- moderating and, subsequently, declining real expenditures on housing, with more doubling up of persons in household units;

- a strong adverse effect on resource industries, construction and many of the types of "core" manufacturing industries concentrated in Ontario (i.e., autos and auto parts, steel, heavy machinery, furniture, rubber and plastics, and primary metal products);

- limited scope for significant, macro-policy initiatives to promote domestic prosperity;

- intensified efforts to formulate and implement industrial policies not likely to be highly successful, especially if slow productivity growth, cost pressures and strong competition combine to produce a relatively high rate of business failures);

- more government intervention and direction of the economy and society;

- increasing difficulties in attracting foreign capital and growing risks that Canadian capital outflows accelerate (perhaps, ultimately, even with net emigration of skilled, professional and managerial people); and

- social tensions and strains of sufficient intensity to give rise to political instability, at least in the sense of relatively frequent changes in governments and more diffuse electoral power across the spectrum of political parties (probably including some new ones).

It is presumed that against this background there will be wider disparities in average living standards between industrially-advanced and less-developed countries (at least the really poor countries, mainly in Africa and Asia, that have not been successful in the past 20 years in starting real growth processes). On the other hand, a growing group of industrializing countries could well achieve relatively rapid growth, even in a low-growth world, and a few of these could reach real average standards of living close to, if not above, those in Canada by the end of the century.

A slow-growing world is also likely to be a world in which East-West tensions are persistent, and, hence, one in which defence spending remains relatively high. Political instabilities and tensions among less-developed countries are also likely to be greater.

3.2/ Prospects for Multinationals in Canada

In these circumstances, there are likely to be conflicting attitudes towards, and pressures upon, multinationals.

On the one hand, with low growth accentuating the needs for more jobs, exports and business investment, the issue of the nationality of the ownership of corporations may well diminish in importance. New foreign investment may be more readily welcomed, and FIRA's tests of "benefits to Canada" may be applied less vigorously if they threaten to deter new foreign investment. The recent tendencies to impose "performance requirements" on foreign-controlled firms may abate. This might particularly be true if the United States and other foreign nations were to begin to press more strongly for Canada to pursue "national treatment" under the OECD guidelines to all established foreign-controlled firms in this country.

On the other hand, the Canadian environment for multinationals could become soured if Canadians perceived that foreign-controlled firms were not dealing even-handedly between their Canadian and foreign operations. Under conditions of persistent 'stagflation' and recurrent economic and financial instabilities, the emergence of such perceptions could happen, which could lead to further steps away from "national treatment" and an escalation of "performance requirements." But, such steps could have adverse effects on the expansion potentials of multinationals and could deter new foreign direct investment.

Similar issues would arise from the fact that under low-growth conditions, the rates of insolvencies, failures, mergers and divestitures would tend to be relatively high. Increased activity in the change of ownership of assets in Canada may sharpen questions about the appropriate role of foreign-controlled business in such activity.

3.3/ Prospects for Multinationals in Ontario

In a low-growth scenario for Canada and the world economy, Ontario would be particularly vulnerable to a loss of economic momentum. Some features would be:

- low productivity performance;
- a loss of competitive capabilities in a variety of established industries;
- a lack of substantial "industrial spillovers" from vigorous investment growth, both in Ontario and other regions in Canada; and
- a relatively high rate of business failures.

In these circumstances, Ontario would not be a highly favourable place for established multinational growth, nor an attractive frontier for new foreign direct investment. The likely response of the Ontario government would be to shift towards a more positive attitude of encouraging multinationals and strengthening industrial policy incentives to attract new industry to Ontario, particularly from the United States.

It would also wish to avert types of federal "performance requirements" or other actions and attitudes that might be inimical to more foreign investment or to foreign takeovers that improve the prospects of survival of existing businesses. The focus would be more on "maximum benefits for Ontario" and less on "maximum benefits for Canada." A low-growth environment, in brief, would accentuate concerns about the health and welfare of the Ontario economy.

Preservation of existing multinational operations would also be a high priority, for example, in the auto, electrical manufacturing, rubber, chemical and machinery fields. These are "core industries" on which a good part of Ontario's economy is based.

Another issue, particularly in this low-growth scenario, concerns the risk that new Canadian multinationals could emerge by developing the leading edges of their expansion in the United States (or elsewhere) under what are perceived to be more favourable opportunities outside Canada. A still greater risk could be that existing Canadian multinationals that already have production bases in the U.S. (and elsewhere) may throw virtually their whole weight of development into expansionary activities outside of Canada.

Specific government actions in Canada to thwart such moves are unlikely to be very successful, and the appropriate basic policy approach should be to maintain a sufficiently favourable domestic environment, and in particular, a favourable Ontario business environment, so that these risks are minimized.

4/ HIGH-GROWTH SCENARIO

4.1/ Key Features

The following key features would likely be reflected in the high-growth scenario, to the year 2000:

- relatively fast growth for Canada as a whole in an international environment of rapid economic growth;

- more stable growth, with short and shallow recessions (mainly reflecting periodic inventory adjustments) and moderate fluctuations in interest rates and capital costs;

- relatively high employment, along with anticipations of occasional pressures on productive capacity, leading to more sustained growth in new business capital investment;

- tough international trade competition, but with less tilt towards trade protection measures than in a low-growth scenario;

- substantial international capital flows in an environment favourable to such flows, with less volatility in international financial markets and exchange rates;

- fairly strong growth in real personal income per capita, real consumer spending and real personal saving;

- adequate increases in government revenues to maintain existing expenditure programmes and, perhaps, even to extend some or introduce new ones;

- improved corporate profits, cash flows and retained earnings favourable to both modernization and expansion of production facilities, enhancing both the quantity and quality of capital per person employed and providing larger opportunities for the implementation and diffusion of new technology;

- moderating growth in new housing expenditures, largely for demographic reasons;

- less erosion in the relative position of goods-producing industries, in general, and of basic resource and core manufacturing industries, in particular;

- less pressure than would exist in a low-growth scenario for government involvement in the formulation and implementation of industrial policies;

- greater attractiveness of Canada as a place for foreign capital investment; and

- greater political and social stability.

In this scenario, while there would still be growing disparities in real living standards between industrially-advanced and less-developed countries (especially the really poor countries in Africa and Asia), there would be greater scope for assisting developing countries through greater trade and aid. At the same time, this world, high-growth scenario would provide a particularly favourable environment for today's newly-industrializing countries focussing on export-led growth. Thus, the present disparities in average standards of living and average productivity levels (especially in manufacturing) between Canada and many of these countries would tend to narrow, perhaps rapidly, before the end of this century.

In such a world environment, East-West tensions could well ease, particularly as the benefits of greater economic linkages and interdependence between Eastern and Western nations were perceived to be growing.

4.2/ Prospects for Multinationals in Canada

This more prosperous and "open" world economic setting would provide, in general, favourable conditions for the growth of multinational organizations. Opportunities would exist for more rapid development and swifter and greater international transfers of new technology in a yeasty environment of new, innovational activities. Multinationals would play a leading

role in expanding world trade. Global product development and marketing would be a growing feature in this kind of world, along with increased specialization and world-scale rationalization of production. International union organization and activities would parallel multinational corporate expansion. Providing immigration rules and regulations permitted, multinationals would tend to become increasingly internationalized in their use of managerial and professional manpower. ("Nationality" would decline, in relative importance, in relation to evaluated "competence.") Greater emphasis would be placed, in this scenario, on competition, in terms of price, quality, delivery dates and many other elements of a more open competitive environment (to the ultimate benefit of consumers). "Political risks" would perhaps be diminished, thus allowing relatively greater scope for assessing and acting upon "economic risks" in the decision-making of multinationals.

In such an environment, conflicting forces would affect such foreign investment screening activities as those operated under FIRA. On the one hand, there would be tendencies not to press the issues of "maximum benefit to Canada" too hard, in the light of the more open options allowing multinationals to consider alternative national locations and "frontiers" for their development. On the other hand, the "prosperity of the multinationals" could well induce, in some respects, an escalation in performance requirements for "entry and expansion" in Canada.

Also, in such an environment, changes in the ownership of assets in Canada would diminish (in terms of the rates of insolvencies, mergers and divestitures), especially under more buoyant conditions for generating corporate cashflows and retained earnings.

Under conditions that would spur countries like Japan to ensure a firm base for needed material, energy and other resources, Canada could find itself, as in the mid-1950s, a country that attracted very substantial multinational resource investment, particularly for firms desiring backward linked vertical integration to assured sources of supply. More generally, Canada could experience a new wave of international economic interdependence, via multinational organizations, that has historically been a feature of rapid growth and development in Canada.

4.3/ Prospects for Multinationals in Ontario

Because Ontario is such a pivotal base of both existing and potential multinationals in the overall Canadian context, Ontario would be affected by the forces and issues that have been outlined for Canada as a whole. But there would likely be some marked differences from the prospects of the low-growth scenario.

In the high-growth scenario, structural change would be more rapid and new technological opportunities much more promising. Therefore, modernization would proceed more quickly, net new business formation would be higher, mergers and acquisitions would be relatively lower, and capacities for risk-taking and new entrepreneurial initiatives would expand. This would provide a favourable environment for growth in new and smaller business units, and multinational activities would undoubtedly reflect these conditions to play a relatively larger role in small- and medium-sized business units.

5/ CONCLUSIONS

In light of the above observations, what conclusions can be drawn about the future of multinational corporations in Canada and, more specifically, in Ontario?

Before attempting to set these out, it would perhaps be appropriate for the author to state some of his personal opinions about a few key elements that influence these conclusions.

- Economic growth of the world, Canada and Ontario will be relatively slow over the 1980s and, possibly, through the 1990s.

- Productivity growth in Canada will be lower than that in many other countries, and lower in Ontario than in the rest of Canada.

- The cumulative impact of such productivity trends will produce a relative decline in average real living standards in Canada vis-a-vis many other countries. (According to crude estimates of such living standards, Canada has fallen from second to about tenth place in international rankings during the 1970s; Canada could wind up well below twentieth place before the end of the century.)

- Average real living standards in Ontario will fall relative to the rest of Canada and are likely to be below the national average within two decades.

- International trade competition will intensify, and Canada and Ontario will lose ground in relative competitiveness, especially for highly-manufactured products.

- Structural economic changes will continue the trends of the past three decades, but these will moderate: relatively, employment will decline in manufacturing, construction and resource industries and rise in the service industries. Even the absolute numbers of employees in manufacturing in Canada could be lower than now by the year 2000, and will almost certainly be lower in Ontario. Most of the increase in employment will occur in small business establishments (with less than 50 employees).

- High unemployment, especially youth unemployment, will be a persistent problem; inflation a more volatile one.

- Financial strains and instabilities in financial markets, both domestically and internationally, will continue; interest rates and exchange rates are likely to fluctuate with substantial amplitudes.

- In the above circumstances, social and political instabilities can be anticipated.

With respect to the future of multinational corporations, a few key conclusions follow.

- Their decisions about where to locate or expand (or contract) their activities will depend (more than usual) upon such basic and central questions as:

  - Where can high growth and high earnings be secured?

  - Where can some of the comparative advantages of such companies be most effectively deployed (i.e., through their capacities for capital mobilization, technological development and diffusion, market penetration, efficient production organization and application of managerial know-how)?

  - Where are costs (of labour, energy, materials and services) likely to be relatively low?

  - Where are tax and regulatory regimes likely to be relatively stable and favourable?

  - Where are "country risks" likely to be relatively low?

- In slower growth and relatively turbulent world economic, social and political conditions, the rate of growth of multinationals will not match the average rate of growth of the past three decades.

- The central focus of their growth will still be in the industrially advanced countries, but there will be growing attention to the relatively high-growth, newly-industrialized countries.

- There will be relative growth in multinational activities originating from some of today's more advanced <u>developing</u> countries, but taken together, these will not be a very significant proportion of world-wide, multinational activities in this century.

- Neither Canada nor Ontario are likely to be strongly attractive locations for foreign multinationals, and other locations will tend to become relatively more attractive for Canadian multinationals (existing and potential).

6/ POLICY IMPLICATIONS FOR ONTARIO

In order to achieve as well performing an Ontario economy as possible, Ontario should seek to maintain a favourable environment for multinational activities. This implies, among other things, maintaining a relatively stable tax and regulatory regime.

Since the most serious potential threat to economic sovereignty and freedom of decision of national policies is a chronic shortage of foreign exchange, Ontario must strongly support activities that help to generate growth in foreign-exchange earnings. The many countries that have sought to achieve this through policies favouring "import substitution" or "domestic content" have not, generally, had a good performance in either economic growth or in the growth of foreign-exchange earnings. Export-oriented growth has been a far more successful route to economic progress. It is, therefore, important for Ontario to be vitally concerned about how to use, as effectively as possible, the capacity of multinationals to push rising production from their Canadian operations through their international marketing systems. Behind this, it is vital to operate policies consistently to maintain relatively open commercial access to U.S. and other international markets.

In a world that is likely to be persistently short of equity capital, and in which the relative strength of business enterprises may increasingly come to depend on their equity capital base, the retention -- indeed, expansion -- of foreign equity investment should be an objective of prime importance, along with keeping Canadian equity capital in Ontario to the maximum possible extent. This will be even more important under conditions of relatively high interest rates. Only enterprises with strong financial positions, including strong balance sheets, will be able to exploit fully new opportunities for business expansion. For the best long-term performance of the Ontario economy, there will have to be a large element of investment-led growth. For this to be possible, there will have to be a high sensitivity in policy to enhance savings and investment processes and, particularly, for a rising volume of savings (both domestic and foreign) to flow into corporations as share capital. (Shares represent an ownership stake and do not require corporations to pay dividends or maintain them in bad times, but the cost of fixed-interest loans or bonds <u>must</u> be paid.)

Another key issue for Ontario to face is how it can strengthen the hands of multinational management searching for promising new mandates or missions for activities in this province. Sensible management in foreign subsidiaries in Canada will probably not be seeking arbitrary "global product mandating," at least in the sense in which this term is normally used. It will be seeking opportunities for solidly-based new missions and mandates believed to have virtue because they can be competitively and profitably developed in Canada. Arbitrary allocation of "global product mandates" is dangerous, it is believed, because "what the Lord giveth, the Lord can take away." Thus, to reinforce an earlier point, it is productivity and competitiveness that lie at the real roots of successful multinational operations in Canada.

Finally, there is a need, in the formulation and the articulation of Ontario policies, to be perceived to welcome and support effective and efficient multinational operations serving the province's long-term, economic performance objectives. This will be important in the context of the rivalry that will exist between Ontario and other provinces, especially for manufacturing activity. But it will also be important in Ontario's "foreign economic relations." Canada is not now perceived to be a favourable location for foreign investment. Indeed, in 1982, the Swiss-based European Management Forum (a non-profit organization, operating under the aegis of the Swiss Federal Council, undertaking research for the OECD and the International Monetary Fund (IMF), and addressing an audience principally consisting of Europeans at the corporate board level) rated Canada in last place among all OECD and six developing countries, in "welcoming foreign investment." Such a perception, if long held, can hardly be a favourable portent for the economic and social progress of this country and of Ontario. For the long-term welfare of Ontario's citizens, it is imperative that careful consideration be devoted now to improving the image of Ontario as a favourable location for future multinational development.

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